No. 512.

IN THE

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1952.

SECURITIES AND EXCHANGE COMMISSION,
Petitioner,

v.

RALSTON PURINA COMPANY.

On Writ of Certiorari to the United States Court of Appeals for the Eighth Circuit.

BRIEF

Of Respondent, Ralston Purina Company.

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Citations.

Cases:

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OPINIONS BELOW.

The opinion of the Court of Appeals (R. 88-99) is reported at 200 Fed. 2d 85. The opinion of the District Court (R. 46-54) is reported in 102 Fed. Supp. 964.

JURISDICTION.

Judgment of the Court of Appeals was entered on November 21, 1952 (R. 100). The jurisdiction of this Court is invoked under 28 U. S. C. 1254. See also Section 22 (a) of the Securities Act of 1933 [15 U. S. C. 77v (a)].

QUESTION PRESENTED AND STATUTE INVOLVED.

The question and the only question before the Court is as to whether the offering of stock here involved, made exclusively to a limited number of "key employees" selected by the Company for sound business reasons, was a private offering and not a public offering within the meaning and intent of the exemption provided in the second clause of Section 4 (1) of the Securities Act of 1933 which provides an exemption from registration for "transactions by an issuer not involving any public offering". Both the District Court and the Court of Appeals for the Eighth Circuit held that the offering of stock here involved was a private offering, not a public offering, and was therefore exempt from registration under the above mentioned provision. This Court thereafter issued its writ of certiorari to review the decision of the Court of Appeals.

STATEMENT.

We feel that it is necessary to make a full statement of this case in order that the Court may have before it as briefly and concisely as possible the evidence which was before the District Court and which was in the Record upon which both the District Court and the Court of Appeals based their decisions, and in the process of doing that, it will be necessary to point out a number of unwarranted and misleading statements found in the Commission's statement in their brief in this Court. We therefore beg the Court's indulgence and careful consideration of the factual situation disclosed by the Record and embodied in the District Court's memorandum of findings and the statements of the Court of Appeals as to what the Record discloses.

The evidence consisted entirely of Exhibits furnished by the Ralston Company at the request of the Commission, with the exception of the oral testimony of Mr. Stuart,

Vice-President and chief financial officer, who was the only witness who testified. And as stated in the Commission's brief, there was no conflict in the evidence.

Ralston Purina Company was organized in 1894. It manufactures and sells mixed feed for poultry and live stock and cereals for human consumption. It had a small beginning, but over the years has grown into a large and very successful company so that it operates 36 feed mills, 6 soy bean processing plants, 3 cereal plants, many warehouses and grain elevators, and 79 retail feed and farm supply stores. Approximately 7,000 people are employed, and net sales for the fiscal year ended September 30, 1951, exceeded $340,000,000 (R. 57).

The Company has had complete continuity of management and from its inception has drawn its executives and managers of its various branch stores and plants around the country, almost exclusively from within its own organization (R. 57).

For a long period of years the Company has followed a settled policy of encouraging ownership of its stock by persons who were regarded and classified by the Company as being "key employees". It first sold stock to such "key employees" in 1911 and particularly since 1942 has made stock ownership available to employees who met its test of being "key employees". In recent years, beginning in 1942, the Company at the end of its fiscal year has paid what was called a "President's bonus" in large amounts to its employees. The total bonus so paid between 1942 and 1951 was approximately $6;354,000, the last bonus in 1951 being in the amount of $1,575,000 paid to 674 employees (R. 59). This bonus was paid only to "key employees". It is not a fact, as suggested in appellant's brief both here and below, that there was any direct relationship between the payment of these bonuses and the stock offerings. No employee was urged or encouraged to invest his

bonus, or any part thereof, in the Company's stock, and certainly no one was required to do so. And there was no pressure of any kind on any employee receiving a bonus to buy such stock. The sole connection between the bonus and the stock offerings was that the payment of the bonus put the individuals in funds to purchase stock if they so wished. The reasons which prompted the Company to wish to sell stock to its key employees were briefly and clearly stated by Mr. Stuart when, in answer to a question as to why the Company so desired, Mr. Stuart testified (R. 58):

> "We feel, sir, that that creates a greater efficiency with the company, because it draws employees of the company closer together. Many of our people come from the rural area, where proprietorship is a matter of great pride to them. The fact that they feel that they are owners, at least part owners, in the company, contributes to the morale, and we feel that the idea of breaking down the gap between the ownership and management is something that is highly desirable and something that contributed substantially to the success of the company."

The evidence shows beyond question that the "key employees" who purchased stock from the Company bought it as an investment and not for the purpose of resale. Of the employees who purchased in 1947, only 7 made subsequent sales. None of the 1948 purchasers sold any stock. Nine of those who bought such stock in 1949 thereafter sold, and 4 of those who bought in 1950 thereafter sold the stock so purchased. Except in 10 instances, the employees who sold had left the Company at the time of the sale. Of the 10 instances above mentioned, 5 had retired or bought homes and the reasons for the remaining 5 sales are unknown. No employee who purchased such stock has ever made any complaint in regard to his purchase (R. 44-45).

In 1945 the Company sold $10,000,000 in preferred stock to the general public by a public offering after registration with the Commission and has never at any time sold any of its common stock to the public (R. 64). None of the stock at any time sold by the Company to its "key employees" was for the purpose of bringing money into its treasury. (If that had been the purpose, the Company could have retained in its treasury the approximately $6,354,000 which it had paid out during these years as bonuses.) Mr. Stuart testified that many employees who asked to buy stock had been turned down and many had had their applications materially reduced (R. 61). All sales to the "key employees" were at all times made for the purpose of obtaining stock ownership by certain selected employees for the purpose and in the manner hereinabove stated.

All sales of such stock to "key employees" were made pursuant to resolution of the Board of Directors and the resolution of the Board authorizing such sale in 1951 is set forth verbatim on page 4 of the Commission's brief. This resolution was communicated to the Company's branch and store managers by intra-company memoranda, and the responsibility to determine the "key employees" who would have an opportunity to purchase stock and the number of shares which they might purchase was delegated to those managers who had supervision over and direct contact with a substantial number of employees. However, their selection of the employees who would be entitled to buy was subject to consultation with and approval by the top executives (R. 58). As the trial court found, the managers were depended upon to select "key employees" after the Company executives had conferred with the managers and outlined the matters to be considered in making selections (R. 47). After the "key employees" to whom stock was to be made available had been selected and the number of shares to be made avail-

able to each employee had been determined, the stock was made available to such employees in response to their respective requests. From time to time employees who were not "key employees" were helped in making purchases, not from the Company, but on the open over-the-counter market.

It will be noted that the resolution, itself, does not specify that the stock is to be sold only to "key employees" and the Commission argued below and argues here that the record indicates that the idea of "sales to key employees" was an afterthought. The District Court's opinion, however, disposes of this argument very thoroughly where the Court said, in referring to it, that the resolution was the same type of resolution that the Ralston Company had used for like offerings in previous years and pointed out that the resolution was not the offering, but merely the authority for the offering, and that in fact the offering so authorized by such resolutions **were limited in every instance to employees who had been classified by the Ralston Company as "key employees"** (R. 54).

The testimony of Mr. Stuart as to what Ralston Company meant by the term, "key employees", was

> "Those who were officers, department heads, assistants to department heads, or other employees whom the Company considered eligible for future promotion to positions of greater responsibility in the administrative, production, personnel, advertising, sales, or research departments—one who was ambitious and likely to develop and grow with the Company's business and who exercised special influence on other employees and was a leader and advisor to other employees, and was sympathetic to management."

This definition was approved by the District Court as to what the Company meant by the expression "key employees" (R. 47).

When Mr. Stuart was asked on cross-examination to clarify his testimony in respect to what was meant by "key employees" as being employees who are ambitious, sympathetic to management, and who advised others, he said (R. 61):

> "Mr. Stuart said that proportionately very few of the key people occupied very subordinate positions in the company. Mr. Sugrue asked, 'In any event, these securities are offered to certain persons occupying very low positions in the company's personnel structure?' Mr. Stuart responded, 'I don't like that word low. They are important people. We are thinking of them as people. They are not big wheels, if you are referring to the big wheels of an organization, but they are key people.' "

The Ralston Company common stock is unlisted, but was dealt in to a limited extent in the over-the-counter market in St. Louis. It was stipulated (R. 9) that over-the-counter sales of this stock to ultimate purchasers for the month of September in each year, 1947 to 1951, inclusive, were fairly representative of such sales for the full year, and the District Court's memorandum opinion (R. 47) set out a brief table showing the yearly sales by the Company in the over-the-counter market to "key employees," compared with sales in the over-the-counter market to the public, as follows:

Year	Yearly Over-the-Counter Sales (Based on September Sales of Each Year) Number of Shares	Yearly Sales to "Key" Employees Number of Shares
1947	8,844	243
1948	1,200	1,120
1949	3,204	10,000
1950	8,544	9,659
1951	11,184	3,763 (applications)

And again on the same question as to what the Company meant by "key employees," Mr. Stuart, on cross-examination, said (R. 61):

"Well, sir, I think that is a matter of influence. I think all of us who have handled people know that there are key people in the various echelons if you have been in military service there were a captain, who perhaps would have felt that one of the lieutenants was a key lieutenant, but you know if you did not have the support of your key sergeant, or the key corporal, or maybe the key private who exercised influence, that you better not go into anything that is very serious; and the same is true in business. Key people are simply not regimented into charts. We don't regiment people in that manner."

The reason for the Company's selling its stock directly to its "key employees" was that if such employees attempted to make like purchases in the limited over-the-counter market, such demand would force the price up artificially (R. 48).

More than 75% of the "key employees" to whom bonuses were paid and to whom stock was offered were already stockholders of the Company* (R. 92). Since 1945 the Company has published a regular annual financial statement which was sent to all of the stockholders, furnished to banks and brokers more or less generally, and filed with the Securities and Exchange Commission, so that approximately 75% of the employees to whom the offering was made were familiar with the Company's sales, profits, general operations, and financial position through such statements (R. 92). And in addition, bi-monthly sales and production records were sent to all the "key" people of

* Of the key employees who purchased stock in the years 1947 to 1950, and who requested an opportunity to purchase in 1951, the following percentage were previously stockholders of the Company (R. 11, 18, 19, 29, 39):

1947	77%
1948	90%
1949	64%
1950	73%
1951	83%

the Company and were available to any employee, so that any such "key employees" who might want to purchase such stock had the information from such statements. And, as testified by Mr. Stuart, tonnage and volume production shown on such statements was the biggest single factor in the Company's success (R. 63).

The Commission's brief undertakes to disparage the value of the information furnished to employees by these bi-monthly statements which show the Company's sales and production records, and argues (Commission's brief, page 12) that it does not follow that the ratio between production and profits is constant, and quotes an article from the Wall Street Journal of December 15, 1951 (R. 63, 82), which stated: "Despite a 35% jump in sales, net income of Ralston Purina Co. for the fiscal year ended September 30 fell to $8,784,341, from the $12,560,665 reported for the preceding year." The Commission's brief, however, completely ignores the fact which was disclosed by this same Exhibit that not only had the sales of the Company jumped from $253,000,000 in 1950 to $342,000,000 in 1951, but, as also shown by its Exhibit, the net income before taxes had increased from $12,560,665 in 1950 to $20,794,065 in 1951, an increase of approximately $8,000,000 in net profits before taxes. That same Exhibit also shows that the impact on income of excess profits taxes had jumped from $8,233,400 in 1950 to $15,369,000 in 1951, plus additional excess profits taxes from the year 1950 of $500,000, so that, except for taxes, both the Company's sales and tonnage had risen by about 35%, and it was only the heavy increase of excess profits taxes which resulted in substantial fall in the final net profit. It appears, therefore, from the Commission's own Exhibit that the sales and tonnage figures, which were given bi-monthly to the employees, did indicate very clearly continued great progress which was affected only by the impact of excess profits taxes.

ARGUMENT.

Both in the District Court and in the Court of Appeals, the Commission based it contention that the offering here involved was a public offering and not private very largely upon two arguments: the Committee reports in connection with the passage of the Securities Act and amendments thereto and administrative rulings of the Commission. We will take these two arguments up in their order.

The Legislative History Does Not Support the Commission's Construction of the Exemption.

As to the argument based on the legislative history, the District Court said (R. 49):

"We are urged to follow these extra-statutory pronouncements in determining the meaning of the statute. The practice does not appeal to us. We think it should be resorted to only in cases of extreme necessity when the recognized rules for statutory construction fail of their purpose. Language used by Congressional Committees is often loose. That observations of Congresional Committees will thereafter be used by the Courts to determine the meaning of laws passed by Congress cannot be said to have been in the minds of the Committee at the time of their pronouncements. Congress does not purposely pass a vague law. Committee declarations are not intended to be used for the purpose of determining the meaning of Congressional Acts by Congress. They do not represent any expression of either House of Congress. Committees of the two Houses may not agree upon the conclusions to be placed upon their actions. The latter is the case here. In 1934 the Securities Act was amended. At that time a proposal was made in the House to exempt stock issue sold to employees of

the issuer. In Conference Report the House managers of the bill stated as a reason for rejection of the amendment:

" '(employees) may be in as great need of the protection afforded by availability of information concerning the issuer for which they work as are most other members of the public.'

"But when the same amendment was before the Senate the author of a like Senate amendment had the following colloquy with a member of the Senate Committee which considered the amendment:

" 'I agree that when the Senator submitted his proposed amendment it struck me as being entirely reasonable, fair and just. I took it that way. And I can see what he proposes in a favorable light. But when the bill went to conference the House Conferees insisted that there was, first, no reason for the amendment * * *

" 'The contention was, and it seems to me that it is almost unanswerable, that an offering to employees solely, as provided in the Senator's amendment, is not a public offering. The argument was made that there was no occasion for this amendment, because under the law there would not be a public offering when the stock was offered simply and solely to employees. And that was the effect of the Senator's amendment. His amendment is limited, as will be seen by its language, which is—

" 'The term "public offering" shall not be deemed to include an offering made solely to the employees.'

" 'I do not believe under the law it really does.'

"**Senator Hastings**: May I inquire—and I make this inquiry because it may be helpful in the future—whether the Senator can say that that was the judgment of the conference itself, or is he speaking only for himself?

"**Senator Fletcher**: Yes; that is the judgment of the conference itself; that there is no reason why employees should not subscribe for stock, and stock be subscribed for by employees under the law as it is. And certainly there is no question in the world that that the Commission has the authority to declare that such an offering would not be a public one."

As the foregoing quotation clearly indicates, Senator Fletcher was speaking not merely as a member of, but for the Conference Committee.

And the Court of Appeals in its opinion, also discussing the legislative history of Section 4 (1) of the Act, reached the same conclusion as Judge Hulen and said (R. 96):

"Assuming, however, that recourse properly may be had to the legislative history of Section 4 (1) of the Act, we agree with the District Court that there is nothing in that history which demonstrates that the offerings in suit do not fall within the exemption provided by that Section."

We have discussed this question of the legislative history for the reason that it points up the basic problem to be here solved. It indicates very clearly that the employer-employee relationship, while by no means the only factor, is a material factor in determining whether or not the offering of securities here involved is a public or a private offering. We ask the Court to understand, however, that we do not contend that an offering made by a company to all of its employees, irrespective of all the other circumstances suronding the offering, the purpose of the offering, and all the other circumstances and considerations that existed in this case, is exempt from registration. What we contended below and what we contend here is that under all the circumstances, that is, the special class of employees to whom the offering was made; the legitimate and mutually desirable purpose sought to be accom-

plished by the Ralston Company and the past history of similar offerings over a long period of time; the lack of solicitation of any kind; the fact clearly shown that no redistribution would be involved; the absence of solicitation or payment of any commissions to anyone; that more than 75% were already stockholders and all received bi-monthly progress reports; all show a private offering and not a public one.

President Roosevelt, in his message initiating this legislation, said that "the purpose of the legislation, I suggest, is to protect the public **with the least possible interference to honest business.**" (Emphasis supplied.) (See note 13, page 20, of the Commission's brief.) The opinion of the Court of Appeals specifically said that its opinion was strictly confined to the precise facts here involved and that the opinion is not to be taken as a ruling that employee stock investment plans are generally within the exemption (R. 99); and that "there is, we think, virtually no possibility that these offerings, if continued, would frustrate or impair the purpose of the Act" (R. 98). We submit that, **in view of the express declaration by the Court of Appeals that its opinion was strictly limited to the precise facts** shown by this record, that a reversal of the Court of Appeals would be a serious interference with the operations of an "honest business" and, on the other hand, an affirmance would not interfere with the accomplishment of the purposes of the Act.

There Has Been No Administrative Construction by the Commission Other Than the Opinion of Its Counsel (Release No. 285) and That Opinion Specifically Recognizes the Particular Factors Which Support Our Contention That the Offering Here Involved Was Private and Not Public.

In the Commission's petition for certiorari, the second ground on which the writ was sought was that the opinion

of the Court of Appeals reversed "a long-standing administrative interpretation". Nowhere in the Commission's brief in the Court of Appeals nor here does it say what that "long-standing administrative interpretation" was, except that in the Court of Appeals the Commission set out in full as an appendix to its brief its Release No. 285 dated January 24, 1935, 11 Fed. Reg., page 10952. That Release was a lengthy opinion by the then counsel for the Commission discussing the question of what was meant by the term "public offering". That release is not set out in the Commission's brief here, but appears in full in the opinion of the Court of Appeals (R. 96-100). That opinion of the Commission's general counsel mentioned and discussed the factors which should be considered in determining whether a public or private offering was involved.

The Commission's counsel said "again in determining what constitutes a substantial number of offerees, the basis on which the offerees are selected is of the greatest importance. Thus an offering to a given number of persons chosen from the general public on the ground that they are possible purchasers may be a public offering **even though an offering to a larger number of persons who are all the members of a particular class, membership in which may be determined by the application of some pre-existing standard, would be a non-public offering.**" And so we see here that the offering here involved was to the members of a particular class (i. e., selected key employees) and that membership in this class was and had been determined for many years past by the Ralston Company by the application of a pre-existing standard; that is, that the offering was limited to persons classified as "key employees."

Another factor mentioned in the opinion of the Commission's counsel was as follows: "I also regard as significant the relationship between the issuer and the offerees. Thus an offering to the members of a class who should have

special knowledge of the issuer is less likely to be a public offering than is an offering to the members of a class of the same size who do not have this advantage. This factor would be particularly important in offerings to employees where a class of high executive officers would have a special relationship to the issuer which subordinate employees would not enjoy." In the instant case the offering was not limited to a favored group of "high executive officers." As the trial court found, such a limited offering would not have accomplished the Company's purpose of bringing from the ranks those who represented good prospects for Company management. But it was limited to a special class of key employees, which included top executives and also those likely to rise in the Company to top executive jobs. And more important, this special class of key employees, 83% of them already stockholders and all of them having the benefit of detailed knowledge as to sales and production, certainly bore a "special relationship to the issuer."

The opinion then discusses the number of units offered and says that the purpose of the exemption of the non-public offerings would appear to have been to make registration unnecessary in those cases where the transaction was of such a nature that the securities in question were not likely to be redistributed or come into the hands of the general public (R. 98). And the record here shows without contradiction that the offerings and the purchases were all made for the purpose of investment by the key employees and not for resale to the public, there only having been 20 sales of stock so purchased in 1947-1950 and these sales were made solely for personal reasons of the individual employees who sold (R. 44-45).

Another factor mentioned in the counsel's opinion was that transactions effected by direct negotiation by the issuer were much more likely to be non-public than those

effected through the machinery of public distribution. The whole tenor of the counsel's opinion was that the determination of a private or public offering was to be from the particular facts and circumstances involved in each case and that no hard and fast rule could be laid down and that each case would have to be determined on that basis.

And the Commission in its Release No. 3439 of May 1, 1952, in the matter of Cristina Copper Mines, Inc, (CCH Fed. Sec. Law. Rep., Sec. 76113, p. 78914), pointed out, as part of the reason for not approving a registration statement, that the offering in question was not confined to stockholders and was not limited to those having any special interest or familiarity with the Company, and that most of the 28,000 shares which Cristina sold were sold to 7 persons and were resold in smaller units shortly thereafter. This Cristina decision by the Commission recognized and reaffirmed counsel's opinion in Release No. 285 as to the importance of the relationship of the offerees to each other and to the issuer and the importance of the question as to whether a resale or redistribution was contemplated after the initial sale The words used by Congress, "a public offering" and "not a public offering," are not words of art. Congress could, if it had so desired, have specified standards and definitions of the word "public." It did not choose to do so, and apparently intended that the question of whether an offering was public or non-public should be determined upon the particular facts involved in each case. It is significant in how few cases the courts have been called upon to construe this expression, "not a public offering." The Sunbeam case, hereinafter discussed, and the instant case are the only two cases in the courts of appeal which are in point; and the decision of the Tennessee District Court in the case of Securities and Exchange Commission v. Federal Compress and Warehouse Company (which we will hereafter

briefly discuss), constitute the only three cases which we know of which are of help on this question.

In discussing the question as to whether the number of offerees involved in any particular offering was a determining factor, the District Court in its opinion said this (R. 53):

> "We take it from the tenor of plaintiff's brief that if defendant had restricted its selection of 'key employees' to less than 100, plaintiff would have no objections to the stock-offering as being a private one. Thus the issue is narrowed—is the stock-offering a public one because made to not to exceed 500 rather than not to exceed 100, out of 7,000 employees. To rule that it is would result in an arbitrary holding that any stock-offering made to offerees in excess of 100 would be public. Neither the statute nor any Congressional report suggests such a standard. It appears to have originated solely with plaintiff."

We have not been advised and do not know of any rule or regulation promulgated by the Commission stating that the offerees must be limited to any specific number and that if not so limited, a public offering would be involved.

The Commission's brief, both in the lower courts and again here, cites a number of cases to the effect that the Commission's administrative interpretations are to be given great weight by the courts. We point out, however, in the first place, that the only interpretation cited or referred to by the Commission is an advisory opinion written by the Commission's former general counsel giving his opinion as to the factors which should be considered in determining whether or not an offering is public or private. And when the Commission speaks in its brief about the interpretation placed upon the law by the Commission (other than the counsel's opinion which we have discussed

at length above), it must refer to individualized interpretations issued, so far as respondent is advised, by some member of the administrative body's staff, unpublished and unavailable to the public and applicable necessarily only to the particular case presented to the Commission. We think we have pointed out that, even treating the opinion of the Commission's counsel, above referred to, as "an administrative interpretation," there is nothing in that opinion that is overruled or even contradicted by the two opinions of the lower courts here involved. On the contrary, both of the lower courts discussed and made applicable to this case a number of the specific points put forth and discussed by the Commission's counsel, and applied them to the facts in the instant case. The court will note that the interpretation of a rule or regulation of the Commission is not here involved. There has been no rule or regulation adopted or promulgated by the Commission which touches the question here involved. The question here presented is the interpretation of the meaning of the statute itself. And the interpretation of a statute by an administrative body is a very different thing from an interpretation of a rule or regulation promulgated by an administrative body. This distinction is shown by the statement of Mr. Justice Brandeis in Norwegian Nitrogen Products Company v. United States, 288 U. S. 294, l. c. 325, in which he said, in referring to the Federal Tariff Commission: "The Commission **was without competence by any decision it might make to fix the meaning of the phrase involved as used by Congress or the courts.** It had power, however, to interpret its own rules and any phrase contained in them." (Emphasis supplied.) It is for the courts and not for the Commission to construe and apply the meaning of "public offering" as applied to the facts in any particular case.

The Decision of the Eighth Circuit Here Involved Is Not in Conflict With the Sunbeam Case.

We pass now to the contention that the decision of the Court of Appeals in the instant case is in conflict with the case of Securities and Exchange Commission v. Sunbeam Gold Mining Company, 95 Fed. 2d 699, decided by the Ninth Circuit Court of Appeals in 1938. That case was strongly relied upon by the Commission in its brief and argument both in the District Court and in the Court of Appeals and was fully considered and distinguished by both the lower courts. The Sunbeam case was an appeal from an unreported decision of the District Court. The Sunbeam Company was a Nevada corporation with stockholders in various states of the Union. It entered into an agreement with another company, the Golden West Consolidated Mines, to purchase or acquire through merger all the assets of the latter company. While the agreement was pending the Sunbeam Company issued through the mails letters to 530 persons, 115 of whom were its own stockholders, 207 were stockholders of Golden West, and 208 were stockholders of both corporations. These letters solicited pledge loan agreements for the purpose of completing the purchase by Sunbeam of the Golden West assets and to raise money to register a contemplated new issue of stock with the Securities and Exchange Commission. Upon signing the pledge loan agreement, the stockholder was to receive "a shareholder's receipt," stated by the court to be in effect a promissory note of Sunbeam, and, therefore, a security. The Commission brought suit to restrain the consummation of the issuance of these loan receipts. The lower court denied the injunction and the Commission appealed. In the Appellate Court it was contended by the Sunbeam Company (l. c. 701) that the phrase, "public offering," has but a single, clear meaning and that it is, in effect, equivalent to an offer to every one. Hence, it was claimed that the re-

striction of an offer to a particular group of persons, such as that of the 323 stockholders of the offering company and the 207 stockholders of the company sought to be merged with the offerer, must be a private rather than a public offering.

In the Court of Appeals in this case, at page 21 of their brief, the Commission referred to their brief the Sunbeam case, which stated: "Obviously, the number of persons to whom the offering is made is a vital factor, and if that number is large it may be unnecessary to consider any other elements." That brief also stated that the large number (530) involved "is of itself sufficient to compel the conclusion that the offering is public in character." The Court of Appeals in the Sunbeam case rejected the contention of the Sunbeam Company that the phrase, "public offering," was in effect equivalent to an offer to everyone. It is significant, however, that in its opinion in the Sunbeam case the Court of Appeals gave no consideration whatever to, and completely ignored the Commission's contention that the number alone was sufficient to make the offering a public one. It is also significant that neither in the Court of Appeals nor in its brief here has the Commission again advanced the claim that the number here involved is of itself sufficient to compel the conclusion that the offering was public.

In refusing to accept the contention which was made by the Sunbeam Company, the Ninth Circuit said (l. c. 701):

> "We cannot accept this contention. On the contrary, we agree with the view of the appellant that the word public 'is one familiar to everyone, but of the most varied and indefinite connotations. In its broadest meaning the term "public" distinguishes the populace at large from groups of individual members of the public segregated because of some common interest or

characteristic. Yet such a distinction is inadequate for practical purposes; manifestly, an offering of securities to all red-headed men, to all residents of Chicago or San Francisco, to all existing stockholders of the General Motors Corporation or the American Telephone & Telegraph Company, is no less "public," in every realistic sense of the word, than an unrestricted offering to the world at large. Such an offering, though not open to everyone who may choose to apply, is nonetheless "public" in character, **for the means used to select the particular individuals to whom the offering is to be made bear no sensible relation to the purposes for which the selection is made.** For the purposes of an offering of securities, red-headed men, residents of San Francisco, and stockholders of General Motors are as much members of the public as their antithetical counterparts. **To determine the distinction between "public" and "private" in any particular context, it is essential to examine the circumstances under which the distinction is sought to be established and to consider the purposes sought to be achieved by such distinction.' "** (Emphasis supplied.)

We do not quarrel with either the principle of that case or the conclusion reached by the Court. The facts there, we submit, are not comparable to those here. There the class of offerees was composed of all the stockholders of two different corporations—one, the offerer, and the other, a prospective vendor—and the offer was to both sets of stockholders for the purpose of raising money by the sale of securities. The District Court in his opinion discussed the Sunbeam case and referred to the statement of the Court in the Sunbeam case where that Court said:

"To determine the distinction between 'public' and 'private' in any particular context, it is essential to examine the circumstances under which the distinction

is sought to be established and to consider the purposes sought to be achieved by such distinction."

And the District Court continued as follows:

"We think this line of reasoning more in harmony with the statute than the arbitrary one of numbers, wholly absent in the Gold Mines case, and which plaintiff now asks this Court to adopt. An examination of the 'circumstances unuder which the distinction is sought to be established' by the defendant and 'the purpose sought to be achieved by such distinction' should be examined. We also consider 'is there a sensible relation to the purpose for which the selection' is made by the employer?" (R. 52).

And later in his opinion Judge Hulen, in referring to the number of the offerees as being the proper test to determine whether an offering was public or private, and in connection with the Sunbeam case, said this: "Neither the statute nor any Congressional report suggests such a standard. It appears to have originated solely with plaintiff" (R. 53).

And Judge Sanborn, in rejecting the contention of the Commission that the opinion of the District Court in this case was in conflict with the Sunbeam case, said (R. 96):

"We do not regard the decision of the District Court in the instant case as inconsistent with the opinion of the Ninth Circuit in the Sunbeam Gold Mines Co. case, the correctness of which as applied to the facts of that case we do not doubt. There are obvious distinctions between an offering of securities to all of the stockholders of two companies, parties to a proposed merger, to raise funds to effectuate the merger, and an offering, without solicitation, of common stock to a selected group of key employees of the issuer, most of whom are already stockholders when the offering is made, with the sole purpose of enabling them to secure

a proprietary interest in the company or to increase the interest already held by them."

There is one other case to which we refer the Court briefly, that is, the case of Securities and Exchange Commission v. Federal Compress and Warehouse Company, an unreported decision of the Tennessee District Court (CCH, Fed. Sec. Law Service, 41-44 Decisions, par. 90,106). In that case the Warehouse Company, in the desire to effect the retirement of its preferred stock, made an offer to its holders of common stock to subscribe to certain treasury stock, the proceeds of such subscription to be paid to a trustee who would then be charged with the duty of using the money to retire the preferred stock. The Commission brought suit for injunction. The trial court dismissed the suit without handing down any formal opinion, but did file extensive findings of fact and conclusions of law.

The Court in that case found that:

> "There was no advertisement of the arrangement, no public solicitation, directly or indirectly, of any one, but it was merely one to be handled by and within the corporate family of stockholders. This one class alone participated therein. No underwriting was required, and there were no underwriters, nor were the services of any brokers, dealers or salesmen sought or obtained. They were not consulted. Nothing was paid in the way of commission or other remuneration, directly or indirectly, for accomplishing the purpose in view."

The Court also said:

> "I also regard as significant the relationship between the issuer and the offerees. Thus, an offering to the members of a class who should have special knowledge of the issuance is less likely to be a public offering than is an offering to the members of a class of the same size who do not have this advantage."

And in referring to what was evidently the opinion of counsel heretofore discussed, the Court said:

> "It is further stated in said release (the opinion of counsel) and recognized that the determination of what constitutes a public offering is essentially a question of fact, in which all surrounding circumstances are of moment; in no sense is the question to be determined exclusively by the number of prospective offerees."

The basic distinction between the Federal Compress case and the Sunbeam case is that in the former the trial court found specifically that it was a material factor in determining the question of the designation, "public", or "private" offering that there was a significant and sensible relationship between the members of the class constituting the offerees and the purpose causing the offeror to make the selection. And in the instant case there is a far closer relationship where the offerees consist solely of key employees 83% of whom were already stockholders and who also had the benefit of information supplied by bi-monthly progress reports heretofore mentioned.

The few other decided cases referred to in the Commission's brief clearly involved a factual situation which was radically different from the situation here, as shown by the record. The English Companies Act contains a similar exemption to the one here involved. The author of the article in 80 Solicitors' Journal 785 (1936), quotes the following from Burrows v. Matabel Gold Reefs and Estates Company (2 Ch. 23):

> "An offer is not the less made to the public because it is made to shareholders and debenture holders as well as to other persons, or because it is not advertised in the public newspapers. But if it is sent solely to the shareholders or debenture holders of the company, there is no offer to the public. The distinction is between the persons who are members or debenture

holders of the company, on the one hand and those who are not, on the other."

We have already referred above, supra, to the Cristina Copper Mines case (Securities Act Release No. 3439, May 1, 1952), where the Commission held that the offering involved was public because it was not confined to stockholders and was not limited to those having any special interest or familiarity with the company. And obviously, Ralston's key employees to whom the offering was made, 83% of whom were already stockholders and received the company's balance sheets every year and had the benefit of the bi-monthly production and tonnage reports, did have special interest in, and familiarity with, the stock which was offered to them.

The Purpose of the Offering.

Mr. Stuart testified, and both Courts found, that the Ralston Company from its inception had had a regular business policy of encouraging stock ownership by its key employees (R. 57). In the earlier part of this brief we set out the reasons for this policy. And again in describing the purpose of the sales, Mr. Stuart said, "We have attempted to have the family remain known as the Purina family, and we call each other very largely 'partner,' and that spirit has been created very largely as a result of this policy of offering stock to a limited group" (R. 60).

We have already shown in our statement that another reason for making the stock available to these key employees from year to year was to avoid their being limited to purchase of stock in the over-the counter market which would have the effect of artificially increasing the price. It was clearly very desirable from the point of view of each employee who wanted stock, to obviate an artificial stimulation of the price in the over-the-counter market. It is not a fact, as suggested in the Commission's brief, that there

was any direct relationship between the payment of bonuses and the stock offerings. No employee was urged or encouraged to invest his bonus, or any part of it, in the Company's stock, and certainly no one was required to do so. The only connection between the bonus and the making available of stock to such key employees was that the bonus put various individuals in funds to purchase stock if they so desired and without an unwarranted price increase. The Company, in making this stock available, was merely protecting its key men.

Further facts should be noted in this connection. There is not even an inference shown in the record that the purpose of any of these offerings in prior years or in 1951 was to raise funds for the Company. As the trial judge said in his opinion, there would be an entirely different situation if any of the circumstances in the case indicated that the Company was using the excuse of a private offering for the purpose of raising funds. This was further made clear by the fact that when the Company did wish to raise money for the purposes of its business it did so by an issue of preferred stock aggregating $10,000,000, and in that instance it went to the public, sold the stock through underwriters, and registered it with the Commission. Mr. Stuart pointed out in his testimony the large expense and the delay and difficulty involved in a registration and the impracticability of such a procedure for the limited offering made to key employees that was here involved (R. 64, 65).

The Number of the Offerees and the Amount of the Offering.

There can be no question as to the number of shares of stock offered in 1951 and the years prior thereto, or as to the dollar amount of the offering. Those facts are covered by the stipulation (Pre-trial conference, Exhibits B, C, D,

E, and F, R. 11-44). The Commission's brief, both in the lower courts and again here, raises an issue as to the number of offerees as opposed to the actual purchasers. Mr. Stuart testified that a complete list of key employees to whom stock was offered was unavailable because the offerings were largely made orally and no complete record of them was kept (R. 8). The testimony showed, however, that the estimated number of offerees in 1951 was 400 to 500 (R. 62). Mr. Stuart said that the figure 500 was only an estimate, that "it was not exactly 500, but was not a thousand, but let us say or any number substantially above that" (R. 62). In reading that testimony on this question it is clear that the words "substantially above that" referred to the figure 500 and not to 1,000. Both the lower courts reached that conclusion and accepted the evidence that the offering was to approximately 500, which was about 5% to 8% of all the Company's employees (R. 47).

Both in the lower courts and again here, the Commission seems to take the position that, in order to qualify as a "key employee" the person must be an important executive with over-all company responsibilities, and not a person who does something like managing a branch store or the other types of work which were done by the key employees. In other words, the Commission claims the right, not only to interpret the words, "public offering," but also attempts to determine for itself what constitutes "key employees." It undertakes to argue, although a company in good faith and with sound business purposes at all times and for a long period of years has determined that a key employee is a person who qualifies under the definition given by Mr. Stuart, that nevertheless the Commission will not recognize such persons as "key employees" because they do not fit its own conception of what it regards as a "key employee."

Unwarranted and Misleading Statements in the Commission's Brief.

At the start of our statement in this brief, we said that it was necessary to point out specifically a number of unwarranted and misleading statements found in the Commission's brief in this Court. If they are allowed to pass unchallenged, this Court might get an entirely erroneous impression of what the facts are as shown in the record and as found by the lower courts.

At the top of page 3 of its brief, the Commission stated that the Company failed to prove that its offering was not made to substantially all of its 7,000 employees. The District Judge found that the offering in question was made in fact to approximately 500, or between 5% to 8% of its employees (R. 47). Mr. Stuart testified without contradiction and the court found it to be a fact, that no offering was made at any time by the Company over this entire period to any employees except those who had been classified by the Company as "key employees" (R. 49).

Again at the bottom of page 10 and the top of page 11 of the Commission's brief, the statement is made that the term "key employee" appears to have included any employee who might have indicated an interest in the purchase of the stock. How can that statement in the Commission's brief be reconciled with the uncontradicted testimony that the Company had never at any time made an offering of stock to any of its employees except those whom it had classified as key employees? On page 10 the Commission's brief makes the conclusion that Mr. Stuart appeared to equate "key employees" to "sales people" and to "production people." There is no evidence to support that conclusion and the Exhibits B, C, D, E, and F referred to above (R. 11-44) show the exact nature of the character of work performed by each one of these key employees. If

a large number of those classified as key employees were salesmen, sales managers, or district sales managers, and production people, both salesmen and production people are extremely important cogs in the Company's operation.

The very surprising statement is made at the top of page 15 that respondent failed to prove that its offering was not made to all of its 7,000 employees. We have already pointed out just above how completely inaccurate that statement is. And substantially the same statement again appears at the end of the first paragraph of the Commission's brief, on page 23. We think it is a fair statement to make that the Commission's brief throughout in this Court (as in the lower courts) attempts to create the impression that the whole idea of making sales of stock to key employees was a subterfuge and merely designed to give color to the Company's contention that this was a private offering and did not have to be registered. And this is done despite the fact that the uncontradicted evidence shows and the lower courts both found that never at any time had the Company sold any of its unissued common stock to the public or to its own employees except to those particular employees whose ties with the Company they wanted to strengthen and who were in good faith and for proper purposes classified by the officers and managers of the Company as "key employees."

CONCLUSION.

We think that the record in this case demonstrates that the decision of the Court of Appeals in this case is not in conflict with the Sunbeam case. We also think that the record shows that the Court of Appeals' decision does not in any way interfere with the accomplishment by the Commission of the purposes of the Act. In this connection we again refer to President Roosevelt's statement when he initiated this legislation that "The purpose was to protect

the public **with the least possible interference with honest business.**" (Emphasis supplied.) If the decisions of the courts below should be reversed, thereby barring a limited amount of stock offerings such as the one involved here, without expensive and impracticable compliance with the registration requirements, it is evident that Ralston could no longer encourage its key employees by giving them the opportunity to become partners in its enterprise. The record in this case shows, and the Commission itself has never even suggested otherwise, that the offering here involved had any element of fraud or imposition, but, on the contrary, was made for sound business reasons following an established practice of many years, which has undoubtedly been one of the factors which has largely contributed to the unusually successful business of the Ralston Company.

We ask this Court to particularly note that in Judge Sanborn's opinion he was careful not to let the decision have the effect of letting the bars down on all stock offerings to employees. On the contrary, in his opinion, Judge Sanborn said that the Court sympathized with the efforts of the Commission, and that the Court was of the opinion that there was no possibility that these offerings, if continued, would frustrate or impair the purpose of the Act (R. 98). He further specifically said:

> "Our opinion is strictly confined to the precise facts here involved, and is not to be taken as a ruling that employees' stock investment plans are generally within the exemption granted by Section 4 (1). If the offerings with which we are concerned were made to all employees or to employees selected at random or by lot or without any logical basis for the selection, a different question would be presented" (R. 99).

Congress was concerned with the problem of weighing the real need for protecting uninformed investors from being "sold" on insufficient knowledge against the equally

substantial need of permitting business to operate free of unnecessary legal or administrative handicaps. And the Congressional safeguard was to place restrictions only where it considered them vital for the protection of the purchasing public. If such restrictions are extended so that they include an offering to a special class composed solely of specified employees of the issuer, who had special knowledge and acquaintance with the issuer's business condition and affairs, then we submit that the balance intended by the lawmakers will be lost. And we submit further that the record in this case provides a clear example of a situation where the purposes of the Act will be served best by maintaining that balance. The stock of Ralston Company was made available, "offered," if you please, solely to a restricted group of its own key employees; and offered to such employees not for the purpose of raising money for the Company, but because management felt that the policy of making such sales to key employees was of the greatest importance in maintaining and building up one of the Company's most important assets—its managerial and administrative manpower; and as the trial court found, the success of the Company testifies to the soundness of that policy. We believe that this is a case of first impression—the first case in which an offering to a restricted class of an issuer's employees has been before the court. We submit that the restrictions on that class imposed by respondent itself were both justifiable and reasonable and the offering to that class is not public within the intendment of the Act. We therefore respectfully urge that the Court affirm the decision of the Court of Appeals.

Respectfully submitted,

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